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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Jurisdictional Separations Reform and Referral to the Federal-State Joint Board	))	CC Docket No. 80-286

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FEDERAL COMMUNICATIONS COMMISSION
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COMMENTS OF U S WEST COMMUNICATIONS, INC.

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March 30, 1999

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List A B C D E

TABLE OF CONTENTS

Page

SUMMARY

U S WEST is encouraged by the Joint Board's State Members' recognition of the deficiencies in current separations procedures and their willingness to consider "fundamental alterations" to the current system such as those proposed by U S WEST. In its earlier comments on Separations Reform, U S WEST urged the Commission to abandon the myriad of complex rules which currently govern the allocation of costs between jurisdictions and establish a "bright line" by assigning all costs from the customers' premises to interexchange carriers' Points of Presence ("POP") to the intrastate jurisdiction. Under U S WEST's proposal, revenues would follow costs and all existing federal revenue streams associated with the recovery of non-traffic sensitive local loop costs and interstate access charge revenues would be reassigned to the state jurisdiction.

Adoption of U S WEST's proposal would eliminate artificial regulatory distinctions and arbitrage opportunities between intrastate and interstate access -- which are essentially the same services using the same facilities. It also would eliminate any need to develop even more complicated separations rules to address the treatment of unbundled network elements ("UNE") and interconnection arrangements.

While the State Members' Report indicates a willingness to consider proposals for comprehensive separations reform, questions continue to arise with respect to the Commission's legal authority and the requirements of Smith v. Illinois Bell. While it serves as the legal and logical underpinning for jurisdictional

separations, U S WEST submits that Smith v. Illinois Bell does not mandate the detailed, burdensome separations process in existence today. Indeed, the case mandates no particular separations process nor does it even require the Commission to engage in separations. Simply put, Smith v. Illinois Bell deals with the limits of state jurisdiction; it does not compel the use of a specific separations methodology nor does it require the Commission to prescribe jurisdictional separations. Moreover, nothing in Smith v. Illinois Bell bars the Commission from relinquishing rate jurisdiction over the multi-use local exchange facilities, as U S WEST suggests in its proposal.

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COMMENTS OF U S WEST COMMUNICATIONS, INC.

U S WEST Communications, Inc. ("U S WEST") hereby responds to the Federal Communications Commission's ("Commission") Public Notice requesting comment on the State Members' Report on Comprehensive Review of Separations ("State Report").[1]

I. INTRODUCTION

In its earlier comments on the Commission's Notice of Proposed Rulemaking ("NPRM") on Jurisdictional Separations Reform,[2] U S WEST proposed that existing separations procedures be reformed dramatically.[3] U S WEST urged the Commission to abandon the myriad of complex rules which are used currently to separate (i.e., allocate) costs of jointly-used facilities between jurisdictions. Rather

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[1] Public Notice, Report Filed By State Members Of Joint Board On Jurisdictional Separations, CC Docket No. 80-286, DA 99-414, rel. Feb. 26, 1999. State Members' Report, CC Docket No. 80-286, rel. Dec. 21, 1998 ("State Report").

[2] In the Matter of Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, Notice of Proposed Rulemaking, 12 FCC Rcd. 22120 (1997) ("NPRM").

[3] See Comments of U S WEST, Inc. filed herein Dec. 10, 1997. Attached hereto as Attachment 1.

than using "traditional" separations rules,[4] the Commission would establish a "bright line" between jurisdictions under U S WEST's proposal by assigning all costs from the customers' premises to the interexchange carriers' Point of Presence ("POP") to the intrastate jurisdiction. Revenues would follow costs and all existing federal revenue streams associated with the recovery of non-traffic sensitive local loop costs (i.e., carrier common line ("CCL"), end user common line ("EUCL"), and primary interexchange carrier charge ("PICC")) and interstate access charge revenues would be reassigned to the state jurisdiction. This would create sufficient jurisdictional symmetry between costs and revenues to satisfy Smith v. Illinois.[5]

Adoption of U S WEST's proposal would eliminate the need for complex separations procedures used today. It would also eliminate artificial regulatory distinctions and arbitrage opportunities between intrastate and interstate access -- which are essentially the same services using the same facilities.[6] Furthermore, it would eliminate any need to develop even more complicated separations rules to address the treatment of unbundled network elements ("UNE") and interconnection arrangements. U S WEST does not believe that a transition period is necessary in order to implement its proposal. In fact, a flash-cut is the preferred approach because transitions have a tendency to become self-perpetuating -- with the final

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[4] It is a myth to claim that existing separations rules reflect cost causation. Rather they reflect the results of sixty years of political compromises which were intended to achieve some predetermined outcome.

[5] Smith v. Illinois Bell Telephone Co., 282 U.S. 133 (1930).

[6] For a more thorough discussion of U S WEST's proposal see U S WEST's Comments (Attachment 1) and Reply Comments of U S WEST, Inc. filed herein Jan. 26, 1998. Attached hereto as Attachment 2.

steps never being taken.[7]

The State Report recognizes that there are deficiencies in the current approach to separations and concludes that the Joint Board should explore "fundamental alterations" to the current system. The State Report specifically references U S WEST's proposal for comprehensive separations reform -- though not endorsing it at the present time.[8] One concern that appears to permeate the State Report is whether the Commission has the requisite legal authority to adopt proposals for comprehensive separations reform such as U S WEST's proposal. While U S WEST believes that earlier comments on the Commission's NPRM fully addressed the question of whether the Commission has sufficient legal authority, U S WEST submits these comments to eliminate any lingering doubts on this issue.

II. THE COMMISSION HAS LEGAL AUTHORITY TO REFORM ITS SEPARATIONS PROCESS AS U S WEST PROPOSES

A. Smith v. Illinois Bell Does Not Require Separations as it is Practiced Today

Smith v. Illinois Bell is the legal precedent which laid the foundation for the Commission's jurisdictional separations process.[9] While it serves as the legal and logical underpinning for jurisdictional separations, U S WEST submits that Smith v. Illinois Bell does not mandate the detailed, burdensome separations process in existence today. Indeed, the case mandates no particular separations

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[7] This is basically the problem with proposals advocating that separations factors be frozen for a certain interim period. U S WEST does not support rule modifications which would freeze existing separations factors.

[8] State Report at 13.

[9] Note 5, supra.

process nor does it even require the Commission to engage in separations. Rather, as subsequent judicial precedent recognizes, the holding of the case dealt only with the limits of state *jurisdiction* over the allocation of costs and facilities associated with interstate communications services.[10]

By way of background, in Smith v. Illinois Bell the Illinois Commerce Commission prescribed telephone rates for the City of Chicago. In establishing its rates, the Illinois Commission did not distinguish "between the intrastate and interstate property and business of the company, but rather based the rates upon the total property and business of the company."[11] Illinois Bell obtained an order from a three-judge Federal District Court panel enjoining enforcement of the prescribed rates and a subsequent federal court found the rates to be confiscatory in violation of the U. S. Constitution. The Supreme Court set aside this judgment on a number of grounds, and remanded the matter to the lower court. In remanding the case, stressing the importance of "the appropriate recognition of the competent governmental authority in each field of regulation," the Court held the interstate service of Illinois Bell to be within federal jurisdiction and confined state regulation to the intrastate business.[12]

The Court then called for further consideration on remand "to the end that by some practical method the different uses of the property may be recognized and the

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[10] See Lone Star Gas Co. v. State of Texas, 304 U.S. 224, 241 (1938); National Ass'n of Reg. Util. Com'rs v. F.C.C., 737 F.2d 1095, 1112 (D.C. Cir. 1984); MCI Telecommunications Corp. v. F.C.C., 750 F.2d 135, 141 (D.C. Cir. 1984).

[11] Smith v. Illinois Bell, 282 U.S. at 146-47.

[12] Id. at 148-49.

return properly attributable to the intrastate service may be ascertained accordingly."[13] While the Court stated that the apportionment did not have to be exact, "it is quite another matter to ignore altogether the actual uses to which the property is put."[14]

It is critical to emphasize that Smith v. Illinois Bell involved no federal action; the Court's concern was action by the state in violation of the U.S. Constitution. The holding of the case is that "interstate tolls are the rates applicable to interstate commerce," and such tolls are not a "matter for the determination either of the Illinois Commission or of the court in dealing with the order of that Commission." Simply put then, Smith v. Illinois Bell deals with the limits of state jurisdiction; it does not compel the use of a specific separations methodology nor does it *require* the Commission to prescribe jurisdictional separations.[15]

It also bears noting that technology and market conditions have changed drastically since Smith v. Illinois Bell. The break-up of the Bell System in the early 1980s fundamentally changed the relationship between local and long distance services that was under consideration in the Smith v. Illinois Bell decision. Further, at the time of Smith v. Illinois Bell, both states and the federal

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[13] Id. at 150-51.

[14] Id. at 151.

[15] Lone Star Gas Co., 304 U.S. at 241 (Characterizing his opinion in Smith v. Illinois Bell, Chief Justice Hughes wrote that the Lone Star decision "was not a case where the segregation of properties and business was essential in order to confine the exercise of state power to its own proper province [citing Smith v. Illinois Bell]."); National Ass'n of Reg. Util. Com'rs v. F.C.C., 737 F.2d at 1112.

government utilized rate-of-return regulation which necessitated the type of strict cost allocations recommended by the Smith v. Illinois Bell court. Today, however, U S WEST and the other large local exchange carriers ("LEC") are primarily regulated under price-cap regulations at both the state and federal levels. Price cap regulation severs the fundamental relationship between cost of service and rates that underlies rate-of-return regulation. Thus, strict cost allocation is no longer necessary in the price cap context. Several commenters to this proceeding have argued that these profound changes in market conditions and technology have rendered Smith v. Illinois Bell an anachronism that is simply no longer controlling.[16] Regardless of the merits of this argument, however, it is clear that the case mandates no particular separations process. Moreover, nothing in Smith v. Illinois Bell bars the Commission from relinquishing rate jurisdiction over the multi-use local exchange facilities.

B. Section 221(c) Does Not Require Separations as it is Practiced Today

Four years after Smith v. Illinois Bell, Congress enacted the Communications Act including Section 221(c). Section 221(c) authorizes the Commission to classify

[16] Comments of GTE Service Corporation filed herein Dec. 10, 1997 at 10-13 ("GTE Comments"); Comments of BellSouth filed herein Dec. 10, 1997 at 2-3 ("BellSouth Comments"); Comments of Century Telephone enterprises, Inc. filed herein Dec. 10, 1997 at 5-7 ("Century Comments"). For example, BellSouth stated: "No formal jurisdictional separations process directly resulted from the *Smith* decision. Indeed, the decision pre-dated the passage of the Communications Act of 1934. Thus, there is no causal relationship between *Smith* and the existing jurisdictional separation rules. Nor can *Smith* be viewed as requiring the Commission to continue to keep jurisdictional separations rules in place." BellSouth Comments at 3.

carrier property and determine the portion of carrier property deemed to be "used in interstate or foreign telephone toll service."[17] If the Commission chooses to establish such classifications, Section 221(c) requires the Commission to do so only after hearings, with notice to the carrier involved, the States in which property of the carrier is located, and other interested persons.[18] In recognition of the interests of States that are affected by separations policies, Section 410(c) grants States an expanded role in separations policy-making by requiring the Commission to refer separations decisions to a federal-state joint board.[19]

It is critical to note that under Section 221(c), the decision to pursue jurisdictional separation in the first place is discretionary with the Commission.[20] The Section 221(c) and 410(c) procedures are mandatory but are triggered only if the Commission elects to exercise its separation authority under Section 221(c).[21] "No procedural requirements are triggered absent the Commission's discretionary

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[17] Section 221(c) provides in pertinent part:

> For purposes of administering this Act as to carriers engaged in wire telephone communication, the Commission *may* classify the property of any such carrier used for wire telephone communication, and determine what property of said carrier shall be considered as used in interstate or foreign telephone toll service.

47 U.S.C. § 221(c) (emphasis supplied).

[18] Id.

[19] 47 U.S.C. § 410(c).

[20] Crockett Telephone Company v. F.C.C., 963 F.2d 1564, 1570 (D.C. Cir. 1992) ("Section 221(c) itself states only that the Commission 'may' institute formal proceedings for the adoption of separation methodologies, not that its 'shall.' As we have noted before, 'the usual presumption [is] that 'may' confers discretion, while 'shall' imposes an obligation to act." (citations omitted)).

[21] Id.

choice to adopt a new formal separation guideline."[22] Thus, on its face, Section 221(c) does not in any way require the Commission to continue its jurisdictional separations according to the existing formulae.

Indeed, the Commission has construed Section 221(c) as simply carrying forward the general goals of the Communications Act regarding the uniform regulation of national communications services.[23] In the Commission's view, the specific objective of Section 221(c) is to "'[obviate] the danger that certain amounts of plant investments and expenses may be assigned to more than one jurisdiction to the detriment of ratepayers.'"[24]

Moreover, the Commission has previously approved the direct assignment of multi-use facilities under Section 221(c) and determined the assignment to be consistent with Smith v. Illinois Bell and later court decisions.[25] In its Mixed-Use Decision, the Commission adopted revised separations rules which directly assigned

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[22] Id.

[23] In the Matter of Southern Bell Telephone & Telegraph Co., Memorandum Opinion and Order, 93 F.C.C. 2d 1287, 1294 ¶ 17 (1983), citing American Telephone & Telegraph Co. & Associated Bell System Cos., 9 F.C.C. 2d 30, 90-91 (1967).

[24] In the Matter of Establishment of Interstate Toll Settlements and Jurisdictional Separations Requiring the Use of Seven Calendar Day Studies by the Florida Public Service Commission, Memorandum Opinion and Order on Reconsideration, 98 F.C.C. 2d 777, 783 (1984).

[25] See MTS and WATS Market Structure, 65 Rad. Reg. 2d (P&F) 1565, 1575-76 ¶ 33 citing Rural Telephone Coalition v. F.C.C., 838 F.2d 1307, 1314-15 (D.C. Cir. 1988) upholding the Commission's decision to use a fixed 25 percent allocation factor in separating subscriber lines and MCI v. F.C.C., 750 F.2d 135 at 141-142 (D.C. Cir. 1984) upholding separations procedures to phase out customer premises equipment. Also see In the Matter of MTS and WATS Market Structure, Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, 4 FCC Rcd. 5660-61 ¶ 7 (1989) ("Mixed-Use Decision").

the costs of mixed-use special access lines to state jurisdictions when these facilities predominantly carried intrastate traffic (i.e., less than 10% interstate traffic).[26] The Commission found that direct assignment fostered administrative simplicity and economic efficiency. In light of the above, it is clear that Section 221(c), like Smith v. Illinois Bell, does not require the continuation of jurisdictional separations as it is currently practiced.

C. U S WEST's Proposal Is Consistent With Smith v. Illinois Bell And Section 221(c)

Most of the telecommunications facilities and associated costs that are subject to separations are mixed-use facilities -- facilities that are used to provide both interstate and intrastate services. There are two general approaches to separating the costs of mixed-use facilities between jurisdictions -- direct assignment or allocation. The vast majority of existing separations rules deal with allocation and the method by which costs are allocated between jurisdictions. U S WEST, however, proposes a direct assignment methodology in which a given mixed-use facility or cost is assigned to either the interstate or intrastate jurisdiction. More specifically, U S WEST proposes that all LEC costs from the customer's premise to the interexchange carrier ("IXC") POP should be assigned to the intrastate jurisdiction. There would be no cost allocation between

[26] Mixed-Use Decision, 4 FCC Rcd. at 5661. In those cases where interstate usage exceeded 10%, the Commission deemed the facilities to be entirely interstate for tariff and cost assignment purposes.

jurisdictions.[27]

U S WEST submits that its proposal is consistent with both Smith v. Illinois Bell and Section 221(c). In U S WEST's view, at most, Smith v. Illinois Bell stands for the proposition that there must be some sort of "jurisdictional symmetry" between revenues and costs. Further, in achieving such symmetry, the Commission must undertake "only reasonable measures"[28] because the "[a]llocation of costs is not a matter for the slide-rule," but "involves judgment on a myriad of facts."[29] Indeed, separations "is not purely an economic issue -- it necessarily involves policy choices that are not constitutionally prescribed."[30] Section 221(c) reflects this flexible approach by granting the Commission discretion over whether to undertake separations and through the fundamental policy focus on protecting ratepayers by ensuring that costs are not assigned to two jurisdictions.

U S WEST's direct assignment proposal is particularly appropriate in light of the "myriad of facts" and "policy choices" involved in the Commission's efforts at jurisdictional separations reform. As U S WEST, GTE and numerous other commenters have previously demonstrated, the current separations rules are outmoded and are not suited to the developing competitive marketplace.[31] Significant improvements in economic efficiency over the existing separations

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[27] There is nothing inherently unfair about the use of direct assignments as long as the revenue streams associated with the use of the particular facilities also flow to the same jurisdiction (i.e., as the direct assignment of costs).

[28] Smith v. Illinois Bell, 282 U.S. at 150.

[29] Colorado Inter. Gas Co. v. Federal Pow. Com'n, 324 U.S. 581, 589 (1945).

[30] MCI Telecommunications Corp. v. F.C.C., 750 F.2d at 141.

program can be achieved through U S WEST's direct assignment proposal. Allocating the costs of commonly-used LEC facilities solely to state jurisdiction will enable states to develop comprehensive and coordinated programs for balancing affordable local service with rational cost recovery in a competitive environment.

Under the U S WEST proposal, revenue streams associated with interstate access would be treated in the same manner as costs that are directly assigned to state jurisdictions -- that is, these revenues would become state revenues. All charges associated with the recovery of non-traffic sensitive local loop costs would move to the state jurisdiction including the current 25% non-traffic sensitive cost federal allocation.

Further, the direct assignment of costs associated with access costs would effectively convert the vast majority of interstate access into intrastate access and would be a major step towards eliminating tariff shopping and rate disparities. The implementation of U S WEST's proposal would inevitably result in interstate and intrastate access services merging into a single service, subject to state jurisdiction.[32] To the extent that the price of intrastate access differed from that of interstate access prior to the merger of these services, the price of the merged service would fall somewhere in between the previous prices. Arbitrage opportunities and pricing disparities which currently arise from the fact that LECs are forced to charge two different prices for what is essentially the same service (i.e., intrastate and interstate access) would disappear with the merger of existing

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[31] See, e.g., Attachment 1, U S WEST Comments at 2-4; GTE Comments at 3-4.

access services.[33]

Simply put then, all parties interconnecting to a LEC's network in the same manner will do so pursuant to a unified and rational rate structure established under a single regulatory regime, rather than the current, bifurcated federal/state regime. In U S WEST's view, this approach would be the most effective method of ensuring competitive neutrality and administrative efficiency in jurisdictional separations, and would ensure that costs are more accurately associated with the cost causers.[34] U S WEST submits therefore that its proposal is consistent with Smith v. Illinois Bell and Section 221(c) and should be adopted.

III. CONCLUSION

For the forgoing reasons, U S WEST believes that the Commission has adequate authority to adopt its proposal. Neither Smith v. Illinois Bell nor the Communications Act are an impediment to reforming separations as U S WEST proposes.

More than a year has passed since the Commission's NPRM was released, no progress has been made in resolving problems with existing separations procedures.

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[32] See Attachment 1, U S WEST Comments at 16.

[33] Adoption of U S WEST's proposal would also eliminate any need for customers to certify how they intend to use the service (i.e., for intrastate or interstate purposes). "Policing" customer usage by service providers has never been very effective and such inquiries are not usually well-received by customers.

[34] See text supra; GTE Comments at 4-7.

It is in the interest of all parties for the Joint Board to move forward expeditiously on separations reform and to give serious consideration to U S WEST's proposal.

Respectfully submitted,

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March 30, 1999

ATTACHMENT 1

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TABLE OF CONTENTS

SUMMARY

With the passage of the 1996 Telecommunications Act and the Eighth Circuit's decision confirming that the states have jurisdiction to establish prices for interconnection and unbundled network elements, it is imperative that separations procedures be reformed dramatically. Rather than adopting even more complex rules to allocate the costs of jointly-used facilities between jurisdictions, the Federal Communications Commission should establish a "bright line" -- assigning all costs from the customer's premises to the interexchange carrier Point of Presence to the intrastate jurisdiction. Concurrently, all revenues generated by services provided over such facilities would also become subject to state jurisdiction. This would eliminate the artificial distinction between intrastate and interstate access -- which are in essence the same service using the same facilities. It also would eliminate any rate disparities and arbitrage opportunities which may exist between interstate and intrastate access services.

Current separations rules reflect policy compromises developed over the last sixty years rather than cost causation. These rules provide little information on the actual cost of providing service in today's increasingly competitive telecommunications market. This problem cannot be remedied by "tinkering" with existing cost allocation procedures. A major overhaul, if not abandonment of existing separations rules, is required. Adoption of U S WEST's separations reform proposal which is contained in the following comments would be a major step

toward eliminating arbitrary jurisdictional cost assignments and insuring that separations procedures reflect economic reality.

In its proposal, U S WEST advocates that all costs associated with commonly-used facilities be directly assigned to either the interstate or intrastate jurisdiction. Under this proposal the vast majority of an incumbent local exchange carrier's facilities would be assigned to the state jurisdiction. In the absence of direct assignment, existing rate disparities between interstate and intrastate access charges will be further exacerbated as carriers begin to purchase unbundled network elements which are subject to state jurisdiction. If the Commission directly assigns all local loop and local switching costs to the intrastate jurisdiction, as U S WEST recommends, it will not be necessary to develop another set of even more complicated separations rules to address the treatment of unbundled network elements and interconnection arrangements.

Neither the Communications Act nor Smith v. Illinois Bell prevents the Commission from adopting U S WEST's proposal. In Smith v. Illinois Bell, the Court held that property, revenues, and expenses had to be separated or apportioned between interstate and intrastate jurisdictions -- but did not require the use of any specific separations methodology. Smith v. Illinois Bell basically stands for the proposition that there must be some sort of "jurisdictional symmetry" between revenues and costs. U S WEST's proposal satisfies this criteria.

Similarly, the Communications Act does not limit the Commission in determining where an interstate call begins or ends or which facilities are identified as being used in the provision of interstate service. In fact, as the Commission observed in its Notice, Section 221(c) gives the Commission the authority to determine what property of a carrier is considered to be used in interstate service. There is no question that the Commission has the requisite legal authority to adopt separations procedures that would result in the direct assignment of all local loop and local switching costs to the intrastate jurisdiction as U S WEST has proposed.

Alternatively, if the Commission declines to revise its separations rules to directly assign local exchange carrier joint-use facilities to the state jurisdiction, the Commission could accomplish the same result by finding local exchange carriers to be connecting carriers in their provision of interstate access service subject to state jurisdiction under 47 U.S.C. Section 152(b) of the Communications Act.

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COMMENTS OF U S WEST, INC.

U S WEST, Inc. ("U S WEST") hereby responds to the Federal Communications Commission's ("Commission") Notice requesting comment on changes that may be needed in its Part 36 jurisdictional separations procedures.[1]

I. INTRODUCTION

U S WEST agrees that separations procedures play an important role in defining the line between federal and state regulation. The question is -- where should the line be drawn? The need for jurisdictional separations of some type should not be confused or equated with a requirement to separate costs in the same manner as has been done historically in the telecommunications industry. Current separations methods have long since outlived their usefulness. Now is the time for dramatic separations reform -- incremental changes are insufficient.

[1] In the Matter of Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, CC Docket No. 80-286, Notice of Proposed Rulemaking, FCC 97-354, rel. Oct. 7, 1997 ("Notice").

With the passage of the 1996 Telecommunications Act[2] and the Eighth Circuit's decision confirming that the states have jurisdiction to establish prices for interconnection and unbundled network elements ("UNE"),[3] it is imperative that separations procedures be reformed dramatically. Commissioner Joan Smith of Oregon recognized this when she stated at a recent Joint Board meeting that:

> "Frankly, rotating the tires on this jalopy is not where I am going. It might make it run a little better in the short term, but we need to look much further ahead to where the market place will value the commodities we now divide the costs of and that surely must be the vision that Congress had in mind . . ." (Federal-State Joint Board on Jurisdictional Separations, Aug. 8, 1997.)

This view appears to be shared by former Chairman Reed Hundt.[4]

U S WEST believes that rather than attempting to allocate the costs of jointly-used facilities between jurisdictions the Commission should establish a "bright line" -- assigning all costs from the customer's premises to the interexchange carrier ("IXC") Point of Presence ("POP") to the intrastate jurisdiction.[5]

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[2] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 ("Telecommunications Act").

[3] Iowa Utilities Bd. v. FCC, 120 F.3d 753, 796-800 (8th Cir. 1997), reh'g granted in part (Oct. 14, 1997), petitions for cert. pending.

[4] At that same Joint Board meeting Chairman Hundt stated that:

> Separations reform ought to be separations abolition. . . . .there is a serious question about whether any time ought to be devoted by the Separations Joint Board to anything that is less than a clear plan to eliminate separations. (Federal-State Joint Board on Jurisdictional Separations, Aug. 8, 1997.)

[5] U S WEST's proposal is the equivalent of a modified "board-to-board" theory of separations with both the costs and revenues associated with the provision of interstate access being assigned to the state jurisdiction. Under this approach, the IXC toll switch and any facilities on the interstate side of this switch which are

Concurrently, all revenues generated by services provided over such facilities would also become subject to state jurisdiction. This would eliminate the artificial distinction between intrastate and interstate access -- which are essentially the same service using the same facilities. It also would eliminate any rate disparities and arbitrage opportunities which may exist between interstate and intrastate access services.

The current approach to separations cannot be sustained in an environment with increasing competition where only one class of providers -- ILECs -- is subject to these arbitrary and overly-complex rules. Separations rules do not apply to competitive local exchange carriers ("CLEC"), wireless carriers, and IXCs including AT&T Corp. ("AT&T") -- all of whom are engaged in the provision of both interstate and intrastate services using common facilities.[6] While the Commission's "traditional" approach to separations may have served both state and federal regulators and the industry well in a monopoly era, it is ill-suited for today's increasingly competitive environment. The fact that the only remaining entities

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currently used in the provision of interstate service would be classified as interstate facilities. The only facilities of incumbent local exchange carriers ("ILEC") that would be assigned to the interstate jurisdiction would be those facilities that are used directly in the provision of interstate service across state lines (e.g., interstate intraLATA service by Regional Bell Operating Companies ("RBOC")).

[6] In the Matter of Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, Order, 11 FCC Rcd. 3271 (1995), Petition for Rulemaking to Reclassify AT&T Corp. as Having Dominant Carrier Status, RM 9006, Order Denying Petition for Rulemaking, FCC 97-366, rel. Oct. 9, 1997.

subject to the current separations rules are the ILECs is all the more reason for the Commission to dramatically reform its separations rules.[7]

II. U S WEST PROPOSAL FOR SEPARATIONS REFORM (Notice ¶ 50)

The Commission's current separations rules engender problems far beyond those associated with jurisdictional cost allocations. Cost allocation, while rarely simple, has become increasingly complex and burdensome as technology evolves and the Commission continues to revise its price cap plan to better accommodate competition.[8] Neither the proverbial "man on the street" nor most

[7] The Commission should not be deterred from dramatically reforming its separations process because it does not have answers to the wide array of "what if" questions which arise at any suggestion that current separations rules might be abandoned or significantly modified. U S WEST is not suggesting that the Commission ignore these details but that it concentrate first on the overall approach to the assignment of costs between jurisdictions. With such an approach the Commission may find that many such seemingly important questions disappear with a major overhaul of separations procedures. Similarly, the Commission should not allow small company concerns to limit separations options. It is no secret that current separations procedures are rife with cross-subsidies, many of which provide universal service support for small local exchange carriers ("LEC"). U S WEST believes that the Commission can move forward with separations reform without harming small LECs by explicitly recognizing separations impacts which affect universal service in the universal service proceeding and by allowing small LECs a significantly longer period of time to adopt any new separations procedures.

[8] The existing separations rules largely evolved in an analog world dominated by "hardware" and are ill-suited to today's "software-dominated" digital environment. For example, many newer telecommunications services employ packet-switching technology. This technology "packages" data into fixed-size packets called cells which are transported within the network over any physical medium. Not all cells contain customer communications and those that do may not be full. Furthermore, it is very unlikely that a message will be transmitted in a continuous stream of cells because cells from many sources are co-mingled and individual message/ communications are disaggregated (into numerous cells) and then are re-assembled after transmission. Thus, it is impossible to equate the number of cells transmitted with a minute of use ("MOU"). Similarly, packet switching has blurred the line between dedicated private line facilities and commonly-used switched transport.

telecommunications professionals have ever heard of SPF (Subscriber Plant Factor), but with price cap reform this esoteric (but very important) separations variable will affect charges to end users.[9] This is just one example of "unheard of" separations factors/rules which can significantly affect ILEC prices depending on how these factors are measured and used in allocating costs.

Without separations in its current form, there would be no need for both interstate and intrastate access -- there would just be access. Similarly, interstate special access and intrastate private line service are essentially the same service and would not exist in the absence of existing separations rules. The existence of what are essentially the same services in both the interstate and intrastate jurisdictions at different prices creates endless opportunities for arbitrage.[10]

Frame relay service ("FRS") is a "switched" private line service which uses packet-switching technology to transport data. From the customer's perspective, FRS functions in the same manner as a dedicated private line even though from an operational perspective it is a switched service.

It is ironic that in one of his last speeches as Commission Chairman, Reed Hundt told the World Affairs Council that "We must not make the same mistakes with the new packet-switched technologies that we have made with our existing circuit-switched network. We must allow competition to build the packet-switched network and allow competitors to operate that network using the technologies and standards that the market favors." Speech as prepared for delivery to the World Affairs Council, Philadelphia, PA, Oct. 22, 1997, From Buenos Aires to Geneva and Beyond at 6. Unfortunately, despite Chairman Hundt's admonition LEC packet-switched networks and services remain subject to comprehensive regulation including the application of out-dated separations rules.

[9] Even though SPF has been frozen at 25% for a number of years, the Commission's new price cap rules recover the non-traffic costs assigned to the interstate jurisdiction by SPF in a different manner than prior rules (i.e., flat per-line charges are replacing usage-sensitive carrier common line ("CCL") charges).

[10] Not to mention the administrative burden on both LECs and regulatory agencies of maintaining separate tariffs for both intrastate and interstate access.

None of the above problems or others can be resolved by minor changes in the current separations rules. Many of these rules reflect policy compromises of decades ago rather than cost causation. Rather than "tinker" with cost allocations, U S WEST advocates the use of direct assignment of all costs associated with commonly-used facilities to either the interstate or intrastate jurisdiction. This "all or none" approach would result in assigning 100% of the cost of a facility to either the intrastate or interstate jurisdiction. Furthermore, U S WEST believes that the demarcation point between interstate and intrastate activities (i.e., for cost assignment purposes) should be the IXC toll switch or its equivalent.[11] Thus, virtually all of an ILEC's facilities would be assigned to the state jurisdiction. The IXC POP and other IXC facilities would be unaffected by this change since IXCs are not subject to the Commission's separations rules. The direct assignment of these facilities, which is discussed in greater detail below, would result in the merger of interstate and intrastate access services under state jurisdiction.[12]

[11] Normally, the demarcation point would be located at an IXC POP. In those cases where an IXC has numerous POPs without switching capacity --"closet" POPs -- in order to minimize LEC access charges, only the IXC POP with switching would be considered in order to determine the demarcation point for jurisdictional separations purposes for LEC facilities. Thus, any dedicated facilities or special access service which an IXC may purchase from a LEC to carry traffic between a "closet" POP and the IXC toll switch would be classified as intrastate under U S WEST's proposal.

[12] Clearly, both Article III, Section 8 of the Constitution and the Communications Act would prohibit state regulatory authorities from exercising their jurisdiction in any way that would burden interstate commerce.

A. Assign Interconnection And UNE Costs To The State Jurisdiction

U S WEST believes that costs associated with interconnection and UNEs should be directly assigned to the intrastate jurisdiction. However, this should only be done in conjunction with the direct assignment of all local loop and access related costs as discussed below. While direct assignment of all such costs to the state jurisdiction would greatly simplify the separations process, direct assignment of only UNE and interconnection costs would result in even more complex and burdensome separations requirements than currently exist.[13] Clearly, if the Commission determines that UNE and interconnection costs should be directly assigned to the state jurisdiction, it logically follows that all local loop and access-related costs should also be assigned to the state jurisdiction since there is no real difference between a UNE (e.g., a local loop) which is used to carry both interstate and intrastate traffic and the UNE when it is bundled with other UNEs to provide a furnished service.

The direct assignment of UNEs and interconnection costs is consistent with the responsibility assigned to the states by the Telecommunications Act as recently

[13] Direct assignment of the costs associated with each individual UNE and interconnection arrangement would require pre-separations adjustments to be made to each separations investment category, depreciation reserve category, deferred tax reserve category, and each operational expense category for each and every type of UNE and interconnection arrangement. It would be necessary to make monthly adjustments for each state based on the volumes of each UNE and interconnection arrangement in service. These amounts would then need to be added manually to state-assigned costs post-separations.

confirmed by the Eighth Circuit's Decision.[14] Assignment of UNE costs to the state jurisdiction also would be consistent with the treatment of private line revenues and costs which are assigned exclusively to either the intrastate or interstate jurisdiction today -- despite the fact that a private line may carry both intrastate and interstate traffic.

B. Assign All Loop Costs To The State Jurisdiction

In addition to the costs of interconnection and UNEs, separations rules should be modified to assign all loop costs to the intrastate jurisdiction -- including the entire cost of those loops used by the ILEC to provide retail basic exchange services. Such an approach would apply a consistent set of regulations to a single multi-use investment. The same loop may be used at different points in time for three different services. For example, an ILEC might use a loop to provide local exchange service to a residential customer. In this case, under current rules the costs of the loop are assigned to both the intrastate and interstate jurisdictions, and cost recovery is the responsibility of two regulators. The same loop could be used in the future by a competitor (i.e., through the purchase of that loop as a UNE) to provide similar retail service to that same customer. In this case it appears that the same loop would be assigned exclusively to the intrastate jurisdiction. Finally, the loop might also be used in the future to provide a private line and, if the private line is used more than 10% for interstate communication, its cost would be assigned exclusively to the interstate jurisdiction.

[14] Iowa Utilities Bd. v. FCC, 120 F.3d at 796-800.

It makes little sense to assign the costs of loop investment differently depending on who provided the service -- the ILEC or a CLEC -- or how the investment is used -- for switched or private line service. The assignment of the loop to the intrastate jurisdiction regardless of the customer or its use would permit a single regulator to address pricing issues associated with the recovery of loop costs. Under U S WEST's proposal, LEC revenues currently derived from interstate CCL and end user common line ("EUCL") charges would be classified as "intrastate" revenues going forward and state commissions would have regulatory oversight of these revenue streams.

This step in separations reform could be accomplished without a lengthy transition. The Joint Board could adopt procedures for such assignment by mid-1998 and establish a date certain for the completion of the change -- but no later than the end of 1998. Individual state regulators, in cooperation with the Commission, could establish their specific plans for the transition during 1998.

C. Assign All Local Switching And Local Transport Costs To The Intrastate Jurisdiction[15]

ILECs' local switching and local transport costs have historically been assigned between the intrastate and interstate jurisdictions based upon the relative use of these investments. With the advent of the Telecommunications Act, these same ILECs' facilities are now available to competitors for use in interconnection and as UNEs at prices established exclusively by state regulators. As stated earlier in these comments, U S WEST believes the costs of such facilities should be assigned exclusively to the intrastate jurisdiction.

U S WEST urges the Commission to eliminate the existing assignment procedures for local switching and local transport costs which vary depending on facility use (i.e., assigned between the state and federal jurisdiction generally, but, exclusively to the state jurisdiction when used for interconnection or UNEs). The

[15] The Commission indicated in its Notice that the assignment of costs associated with LEC implementation of local number portability ("LNP") was beyond the scope of this proceeding. (See Notice ¶ 5). U S WEST assumes that the Commission excluded LNP costs because it has not yet adopted final rules on how these costs will be recovered on a "competitively neutral basis" from all telecommunications carriers, as required by the Act. (See 47 U.S.C. § 251(e)(2)). The fact that the Commission has yet to promulgate cost recovery rules need not delay the decision as to which jurisdiction LNP costs should be assigned. The Telecommunications Act clearly assigns the responsibility for number portability to the Commission. The Commission has: established the deployment schedule for LNP; determined the technology to be used by LECs; and will determine how costs will be recovered from carriers. Given the nonrecurring nature of most LNP costs and the Commission's pervasive control over virtually all aspects of LNP deployment, it would be inappropriate to assign anything other than 100% of these costs to the interstate jurisdiction. U S WEST believes that the most appropriate way to recover these costs is over a three-year transition period. After the completion of this transition period all ongoing LNP costs should be treated the same as any other local switching cost.

disparate dual treatment of the costs of these facilities is particularly inappropriate since, as the Commission itself has noted, UNEs may be purchased as substitutes for local switching and local transport services.[16]

D. Unrecovered Interstate Historical Costs Should Remain With The Commission Until They Are Recovered On A Transitional Basis

The Commission has already recognized that historical cost recovery is an issue that must be addressed as the Telecommunications Act is implemented.[17] There is no question that existing depreciation rates which are based on unrealistic service lives have been inadequate. As a result, LECs' booked costs include costs which have been deferred for future recovery through the use of uneconomic service lives. In the past, with minimal competition in local exchange markets, the Commission, arguably, could claim that the use of uneconomic service lives would not jeopardize LEC recovery of such costs. But even then, the Commission

[16] See generally In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd. 15499 (1996).

[17] In the Matter of Price Cap Performance Review For Local Exchange Carriers, CC Docket No. 94-1, Transport Rate Structure And Pricing, CC Docket No. 91-213, End User Common Line Charges, CC Docket No. 95-72, First Report and Order, 7 Comm. Reg. (P&F) 1209, 1228 ¶ 49 (1997) ("1997 Access Reform Order"), appeals pending sub nom. Southwestern Bell Telephone Co., et al. v. FCC, Nos. 97-2618, et al. (8th Cir.). As former Commission Chairman Reed Hundt stated in his remarks before the August 14, 1997 Joint Board: "Historical cost recovery is not irrelevant and not unimportant. It is necessary to pay for the networks. We do want to have costs incurred in connection with regulatory bargains recovered in a fair way."

recognized the importance of the depreciation reserve deficiency problem and took steps to resolve it.[18]

With increasing competition and the advent of the Telecommunications Act, it is all the more important that the Commission take immediate steps to resolve the depreciation reserve deficiency problem. LECs' ability to recover the costs that they lawfully incurred in the provision of regulated service in prior years is in jeopardy. In fact, U S WEST expects that portions of its network will be removed from service long before the current depreciation lives have expired.[19] Furthermore, the Commission's own policy, as set forth in its 1997 Access Reform Order, is to move ILEC access rates to forward-looking costs within the next four years.[20] To the extent an ILEC's current costs exceed its forward-looking costs, the ILEC should have an opportunity to amortize the difference during a three-year transition. In fact, the Commission has a legal obligation to allow LECs an opportunity to recover these costs.[21]

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[18] In the past, the depreciation reserve issue has been viewed as much a problem caused by rapidly-evolving technology as from competition. In 1988, the Commission allowed carriers to amortize what the Commission believed to be a reasonable approximation of the depreciation reserve deficiency which existed at the time. In the Matter of Amortization of Depreciation Reserve Imbalances of Local Exchange Carriers, Report and Order, 3 FCC Rcd. 984 (1988).

[19] For example, U S WEST is allowed to use a depreciation life of 15.5 years in calculating depreciation rates for its switches. This is considerably longer than the depreciation life that U S WEST uses for financial reporting purposes (i.e., 10 years) or that carriers not subject to the Commission's depreciation rules use (e.g., AT&T uses a depreciation life of 9.7 years).

[20] 1997 Access Reform Order, 7 Comm. Reg. (P&F) at 1279-80 ¶ 267.

[21] Failure to allow recovery of these costs would constitute a taking in violation of the Fifth Amendment.

U S WEST urges the Commission to address this problem in conjunction with separations reform. U S WEST suggests that the Commission allow carriers to amortize the reserve deficiency recovery over a three-year period. This could occur in one of three ways. The preferred way, in U S WEST's view, is to move forward with separations reform (and the assignment of LEC interstate access costs to the intrastate jurisdiction) at the earliest possible date and to adopt a transitional interstate rate element to recover the reserve deficiency. An alternative approach is to delay separations reform for a three-year transition period during which the reserve deficiency is amortized over existing LEC interstate services.[22] A much less desirable alternative is to transfer unrecovered historical costs to the intrastate jurisdiction (i.e., after the creation of a transitional rate element).

E. Universal Service Is A National Concern And Should Be Funded At The Federal Level (Notice ¶¶ 93-95)

The Telecommunications Act requires that implicit support for universal service be removed from LEC rate structures and replaced with "specific, predictable and sufficient" explicit support mechanisms.[23] The size of the high-cost fund which will be necessary to satisfy the Telecommunications Act's universal service requirements has been the subject of much debate with estimates ranging

[22] Any further delay in addressing this problem will greatly increase LECs' risk of never recovering these lawfully incurred costs. These costs were incurred in providing regulated interstate telecommunications service and the Commission may not ignore them. With increasing local competition, much of it arising from the use of under-priced LEC facilities, it will be difficult to recover the under-depreciated costs of past investment unless the Commission acts expeditiously.

[23] 47 U.S.C. § 254(b).

from a low of $6 billion to a high of $20 billion.[24] Once the size of the explicit support requirements for each state is determined, a mechanism must be developed to collect the necessary funds from all telecommunications providers on a competitively neutral basis.[25] U S WEST is of the opinion that universal service is a national goal which should be administered and funded at the national level if glaring inequities are to be avoided between U.S. citizens living in different states.[26]

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[24] The Commission currently has an inquiry underway to develop a cost proxy model which will be used to size the fund and target support to high cost areas. See In the Matter of Federal State Joint Board on Universal Service, Forward-Looking Mechanism for High Cost Support for Non-Rural LECs, CC Docket Nos. 96-45 and 97-160.

[25] 47 U.S.C. § 254(d).

[26] Two primary alternatives have been discussed for raising the necessary funds:

- A National fund, where the total funding requirements across all states are divided by the sum of all intrastate and interstate revenues to compute a common surcharge for intrastate and interstate revenues.
- Separate State and Interstate funds, where 75% of the funding requirements are divided by each state's intrastate revenues to determine a state-specific intrastate surcharge, and the remaining 25% of the funding requirements are divided by total interstate revenues to develop an interstate surcharge.

U S WEST's analysis shows that while a National fund would require a uniform 8% surcharge on all interstate and intrastate telecommunications services, separate State funds to recover 75% of each state's universal service costs would range from a 57% surcharge in South Dakota, to virtually zero in the District of Columbia. For the most part, it is the western and southern states which would have the highest state-specific intrastate surcharges.

In addition to these two distinct approaches for funding universal service, it is possible to employ a "hybrid" approach which would avoid extreme disparities in contributions between states while still allowing for separate state funds. This hybrid approach would establish a "very" high-cost threshold (e.g., $50 per line) above which all additional costs would be funded through a National fund. Per-line costs below this threshold but above the high-cost benchmark (e.g., $30) would be

As such, any surcharge associated with the implementation of the Telecommunications Act's universal service requirements and goals should be determined and levied at the National level.

III. PRICING IMPLICATIONS OF U S WEST'S PROPOSAL (Notice ¶¶ 84-87)

The implementation of U S WEST's separations reform proposal would have a profound impact on the pricing structures of ILECs with only a nominal impact on pricing levels. It is anticipated that revenue streams associated with interstate access would be treated in the same manner as costs that are directly assigned to state jurisdictions -- that is, these revenues would become state revenues.[27] For example, all federal revenue streams (i.e., charges) associated with the recovery of non-traffic sensitive local loop costs would move to the state jurisdiction along with the current 25% non-traffic sensitive ("NTS") cost allocation. This would include: CCL charges, EUCL charges, and newly-adopted Primary Interexchange Carrier Charges ("PICC"). The net result is that all costs and all revenues associated with the use of the local loop would be subject to state jurisdiction.[28] This integration of local loop costs and revenues should help make the task of "rebalancing" local rates

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jointly funded by separate intrastate and interstate funds in the same manner as in the second alternative discussed above.

[27] Clearly, state regulatory commissions have the authority to determine the appropriate price level in most states. However, it is anticipated that if U S WEST's plan were adopted state commissions would leave existing interstate price structures in place until they had an opportunity to examine rates for a "combined" access product.

[28] That is other than universal service subsidies or levies which should continue to be subject to federal jurisdiction in order to best comply with requirements and the intent of the Telecommunications Act.

easier for state public utility commissions as they remove historical subsidies to better reflect competitive conditions with all of the local loop costs subject to state jurisdiction. In the near term, it is unlikely that the implementation of U S WEST's proposal would have anything other than a nominal impact on the prices charged to end users for local service.

The situation is quite different with access services than with the local loop. With the local loop there is basically only one service and a number of revenue streams (i.e., the local rate, usage charges, CCL charges, EUCL charges and PICC charges). Whereas with access there are distinct services for both interstate and intrastate access. Basically these services look the same and essentially use the same facilities but are likely to have different prices (i.e., unless the state jurisdiction allows the ILEC to have "mirrored" rates). With the implementation of U S WEST's proposal, it is inevitable that interstate and intrastate access services would be merged into a single service subject to state jurisdiction.[29] If the price of intrastate access differed from that of interstate access prior to the merger of these

[29] Interstate and intrastate access cannot exist as distinct services in the absence of artificial regulatory constraints. With the elimination of jurisdictional boundaries, competition/arbitrage will lead to a convergence of prices for all access MOUs. The cost to produce an MOU is essentially the same for both interstate and intrastate access over a given route. Furthermore, it is becoming increasingly difficult for LECs to identify whether traffic from a CLEC or IXC is interstate or intrastate traffic. This inability to determine the jurisdictional nature of MOUs highlights the unsustainability of current separations rules which are largely based on measures of relative use. In such an environment, carriers have a financial incentive to identify their traffic as interstate or intrastate on the basis of the price of interstate and intrastate access, not the origination or destination of the traffic. In reality, what should matter is the level of usage -- not whether an MOU is classified as an interstate or intrastate MOU.

services, one would expect the price of the combined service to fall somewhere in between the previous prices. Arbitrage opportunities and pricing disparities would disappear with the merger of existing access services.[30]

In essence, U S WEST's proposal is quite simple. All "local" facility costs would be assigned entirely to the state jurisdiction and revenues would follow. While the access charge structure highlights the need for separations reform such as that proposed by U S WEST, it also allows the Commission to implement this proposal with little if any inconvenience to carriers or customers.

IV. THE COMMISSION HAS SUFFICIENT LEGAL AUTHORITY TO REFORM ITS SEPARATIONS PROCESS AS U S WEST PROPOSES (Notice ¶¶ 32-27)

Neither the Telecommunications Act nor legal precedent require that the Commission continue to use its existing separations process which is a cumbersome, complex product of another era.

A. Smith v. Illinois Bell Does Not Require Separations As We Know It Today (Notice ¶¶ 32-37)

As the Commission notes in its Notice, Smith v. Illinois Bell[31] is the legal precedent which laid the foundation for the interstate/intrastate separations process as we know it today.[32] In Smith v. Illinois Bell, the Court addressed the issue of whether the local rates prescribed by the Illinois Commerce Commission for

[30] Adoption of U S WEST's proposal would also eliminate any need for customers to certify how they intend to use the service (i.e., for intrastate or interstate purposes). "Policing" customer usage by service providers has never been very effective and such inquiries are not usually well-received by customers.

[31] Smith v. Illinois Bell Telephone Co., 282 U.S. 133 (1930) ("Smith v. Illinois Bell").

[32] Notice ¶¶ 32-37.

telephone service in the City of Chicago were confiscatory. In establishing its rates, Illinois Bell employed the "board-to-board" theory of cost assignment, which assigned all local distribution plant and local switching costs to local service regardless of whether these facilities were used in the origination and termination of interstate calls. Only toll switching and interexchange plant costs were assigned to interstate calls. This resulted in the situation where customers were charged interstate rates for "station-to-station" calls (i.e., from the originating telephone set to the receiving or terminating telephone set) but no costs associated with local switching or local distribution were assigned to these calls. Basically interstate calls had a "free ride" on local facilities. While this may appear nonsensical at first glance, it arose in an environment where the parent company, AT&T, was the provider of interstate long distance service and its subsidiary, Illinois Bell, was the provider of local service.

In Smith v. Illinois Bell, the Court held that property, revenues and expenses had to be separated or apportioned between interstate and intrastate jurisdictions.[33] While the Court did not find that apportionment had to be exact, "it is quite another matter to ignore all together the actual uses to which the property is put,"[34] as was the case in Smith v. Illinois Bell. The Court found that the validity of an intrastate rate could not be determined without "an appropriate determination of the value of the property employed in the intrastate business and the compensation receivable

[33] Smith v. Illinois Bell, 282 U.S. at 148-151.

[34] Id. at 151.

for the intrastate service under the rates prescribed."[35] Nowhere in Smith v. Illinois Bell did the Court require the use of a specific separations methodology nor did it require the Interstate Commerce Commission, the Commission's predecessor, or any other authority to prescribe jurisdictional separations.

B. Smith v. Illinois Bell Requires "Jurisdictional Symmetry" Between Costs And Revenues (Notice ¶¶ 32-37)

U S WEST believes that Smith v. Illinois Bell basically stands for the proposition that there must be some sort of "jurisdictional symmetry" between revenues and costs. The case provides no insight into the question of where intrastate costs end and interstate costs begin or vice versa. The Court simply found that it is impossible to determine whether a rate is confiscatory if certain costs associated with providing the service are ignored.

U S WEST believes that "jurisdictional symmetry" between costs and revenues can be achieved (and the requirements of Smith v. Illinois Bell satisfied) in a number of different ways. One way is the Commission's traditional approach to separations which evolved in an environment where AT&T Long Lines was the predominate provider of interstate long distance service and its affiliates, the local Bell Operating Companies ("BOC"), were the predominate providers of intrastate service. This approach to separations was end-to-end (or station-to-station). Costs of virtually every class of commonly-used plant were allocated between jurisdictions on the basis of a variety of factors including relative use, direct assignment, and fixed factors among others. The results of this approach were "less than scientific"

[35] Id. at 149 citing Minnesota Rate Cases, 230 U.S. 352, 435, 33 S. Ct. 729.

and were more often the product of political compromises than reflective of the cost characteristics of telephone plant. Over more than fifty years, traditional separations has evolved into a complex set of rules known more for the use of arcane acronyms such as BAF, SPF and DEM than the rational assignment of costs. It is a system of rules that would make Rube Goldberg proud.[36]

While traditional separations may have had some merit when the Bell System was still whole, it really did not suit the post-divestiture environment where the BOCs largely provided exchange service and interstate service was largely provided by separate entities such as AT&T, Sprint and MCI who owned no local facilities. These companies provided interLATA service by purchasing either interstate or intrastate "access" service. For all intents and purposes, there is no difference between a local exchange company's interstate access and intrastate access. Both services use essentially the same facilities to terminate or originate IXC calls. Interstate access is an interstate service because the Commission has found it to be an interstate service. The Telecommunications Act does not limit the Commission in determining where an interstate call begins or ends or which facilities are identified as being used in the provision of interstate service. In fact, as the Commission observed in its Notice, Section 221(c) gives the Commission the authority to determine what property of a carrier is considered to be used in

[36] Past readers of the comics in Sunday papers found humor in Rube Goldberg's incredibly complex multi-step processes/machines to perform very simple tasks such as turning on a coffee pot.

interstate service.[37]

C. The Commission Has Found Previously That Direct Assignment Of Mixed-Use Facilities Is Lawful (Notice ¶¶ 32-37)

Most of the facilities and associated costs that are subject to separations are mixed-use facilities. That is, facilities that are used to provision both interstate and intrastate services. There are two general approaches to separating the costs of mixed-use facilities between jurisdictions -- direct assignment or allocation. The vast majority of existing separations rules deal with allocation and the method by which costs are allocated between jurisdictions. Direct assignment is much simpler -- the facility or cost is assigned to either the interstate or intrastate jurisdiction. There is no cost allocation between jurisdictions.[38]

The use of direct assignment is particularly appropriate when costs do not vary with usage (i.e., NTS costs). The Commission has found previously that the use of direct assignment is consistent with the Court's decision in Smith v. Illinois Bell and later court decisions.[39] In its Mixed-Use Decision the Commission adopted

[37] Notice ¶ 35; also see 47 U.S.C. § 221(c).

[38] There is nothing inherently unfair about the use of direct assignments as long as the revenue streams associated with the use of the particular facilities also flow to the same jurisdiction (i.e., as the direct assignment of costs).

[39] See In the Matter of MTS and WATS Market Structure, Recommended Decision and Order, 65 Rad. Reg. 2d (P&F) 1565, 1575-76 ¶ 33 citing Rural Telephone Coalition v. FCC, 838 F.2d 1307 at 1315-1315 (D.C. Cir. 1988) upholding the Commission's decision to use a fixed 25 percent allocation factor in separating subscriber lines and MCI v. FCC, 750 F.2d 135 at 141-142 (D.C. Cir. 1984) upholding separations procedures to phase out customer premises equipment. Also see In the Matter of MTS and WATS Market Structure, Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, Decision and Order, 4 FCC Rcd. 5660-61 ¶ 7 (1989) ("Mixed-Use Decision").

revised separations rules which directly assigned the costs of mixed-use special access lines to state jurisdictions when these facilities predominantly carried intrastate traffic (i.e., less than 10% interstate traffic).[40] The Commission found that direct assignment fostered administrative simplicity and economic efficiency.

The Commission has not encountered any legal impediments to the use of direct assignment for mixed-use facilities in the past. There is no question that the Commission has the requisite legal authority to adopt separations procedures that would result in the direct assignment of all local loop and local switching costs to the intrastate jurisdiction as U S WEST has proposed. The direct assignment of these costs would effectively convert the vast majority of interstate access into intrastate access and be a major step towards eliminating tariff shopping and rate disparities.

Under existing separations procedures, many LECs find themselves in the unenviable position of charging two different prices for what is essentially the same service. In the absence of direct assignment, this problem will be further exacerbated as carriers begin to purchase UNEs which are subject to state jurisdiction.[41] If the Commission directly assigns all local loop and local switching costs to the intrastate jurisdiction it will not be necessary to develop another set of separations rules to address the treatment of UNEs.

[40] Mixed-Use Decision, 4 FCC Rcd. 5660. In those cases where interstate usage exceeded 10%, the Commission deemed the facilities to be entirely interstate for tariff and cost assignment purposes.

[41] Iowa Utilities Bd. v. FCC, 120 F.3d at 796-800.

V. IN THE ALTERNATIVE, THE COMMISSION SHOULD CLASSIFY LECS AS CONNECTING CARRIERS IN THEIR PROVISION OF INTERSTATE ACCESS (Notice ¶¶ 50)

Clearly as discussed above, the Commission has the authority to directly assign to state jurisdictions facilities which are jointly used in the provision of both interstate and intrastate services. If for some reason the Commission declines to take such action, it is U S WEST's opinion that the Commission could accomplish the same result by finding LECs to be connecting carriers in their provision of interstate access service subject to state jurisdiction under 47 U.S.C. Section 152(b) of the Communications Act.[42]

In its only post-divestiture proceeding on this issue, the Commission found that any LEC providing "end-to-end" interstate service could not be classified as a connecting carrier for Section 152(b) purposes.[43] The Commission interpreted Section 152(b)'s language very narrowly and found that carriers "engaging in interstate service" in any manner other than "solely through physical connection with the facilities of another carrier" could not fall within the connecting carrier exemption contained in Section 152(b).[44] Under the Commission's decision, a carrier with a single end-to-end interstate facility-- regardless of the size of its other

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[42] 47 U.S.C. § 152(b) ". . . nothing in this [Act] shall be construed to apply or to give the Commission jurisdiction with respect to . . . (2) any carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier . . ."

[43] In the Matter of Declaratory Ruling on the Application of Section 2(b)(2) of the Communications Act of 1934 to Bell Operating Companies, Memorandum Opinion and Order, 2 FCC Rcd. 1750, 1753 ¶ 29 (1987).

[44] See id.

operations -- could not be classified as a connecting carrier subject to state jurisdiction.

U S WEST does not believe that the Commission is compelled to read the statute in such a narrow manner. The language of the statute is not unambiguous and the Commission has the latitude to interpret Section 152(b) in such a manner that LECs are classified as connecting carriers (i.e., subject to state jurisdiction) for purposes of regulating interstate access and differently for purposes of regulating end-to-end interstate service.[45] U S WEST urges the Commission to re-examine the connecting carrier issue.

Classification of ILECs as connecting carriers in their provision of access services would allow all access and interconnection services to be under the jurisdiction of a single regulatory agency. The current bifurcated regulation of access services between state and federal jurisdictions has resulted in both a duplication of services and the unnecessary creation of pricing anomalies. It would be a major step forward in the rationalization of the regulation of communications services to have all access and interconnection services combined under state jurisdiction. Such integration of access services is all the more important with increasing local exchange competition and the increased complexity associated with access reform.

[45] Chevron, U.S.A., Inc. v. Natural Resources Defense, 467 U.S. 837, 843 (1984).

VI. CONCLUSION

U S WEST urges the Commission to reform its separations procedures at the earliest possible date in accordance with the foregoing comments.

Respectfully submitted,

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